

AMENDED IN ASSEMBLY APRIL 19, 2001

AMENDED IN ASSEMBLY APRIL 5, 2001

CALIFORNIA LEGISLATURE—2001–02 REGULAR SESSION

**ASSEMBLY BILL**

**No. 489**

**Introduced by Assembly Member Migden**

February 21, 2001

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An act to add Section 10247.5 to the Business and Professions Code, to add Chapter 7.6 (commencing with Section 1922) to Title 4 of Part 4 of Division 3 of the Civil Code, to add Sections 3398, 7508, 22168, and 50511 to the Financial Code, and to add Section 13984 to the Government Code, relating to residential mortgage lending.

LEGISLATIVE COUNSEL'S DIGEST

AB 489, as amended, Migden. High-cost home equity loans.

Existing law provides for regulation of banks and savings associations by the Department of Financial Institutions. Existing law provides for regulation of real estate brokers by the Department of Real Estate. Existing law provides for regulation of finance lenders and residential mortgage lenders by the Department of Corporations. Existing law provides that willful violations of provisions governing savings associations, real estate brokers, and residential mortgage lenders are crimes.

This bill would require the Secretary of the Business, Transportation and Housing Agency to adopt regulations with respect to the origination of high-cost real estate loans, relative to defining schemes, devices, or contrivances that are manipulative, deceptive, or otherwise fraudulent and to identifying means to curb abusive practices related to the

advertising, brokering, and making of those loans. The regulations would be developed in consultation with the Commissioner of Corporations, the Real Estate Commissioner, the Commissioner of Financial Institutions, and the Attorney General, and the regulations would be enforced by the agencies charged with regulation of specified persons and entities involved in the making of real estate loans.

Because willful violations of these provisions with respect to savings associations, real estate brokers, and residential mortgage lenders would be crimes, this bill would impose a state-mandated local program by creating new crimes.

This bill would also impose various requirements with respect to loan contracts and loan brokerage contracts. A willful violation of these provisions would be a crime and would result in the voiding of the loan contract.

The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: yes.

*The people of the State of California do enact as follows:*

- 1 SECTION 1. The Legislature finds and declares all of the
- 2 following:
- 3 (a) There has been an explosion in the amount of credit made
- 4 available to low-income borrowers in recent years, as a result of
- 5 economic growth, technological changes, and financial
- 6 innovations. A significant portion of this expansion has occurred
- 7 in the subprime lending market, which refers to lending to
- 8 borrowers who do not qualify for prime rates, either because of
- 9 impaired credit histories or low incomes. According to the United
- 10 States Department of the Treasury, subprime lending nationwide
- 11 increased from \$35 billion in 1994 to \$370 billion in 1999.
- 12 (b) Subprime loans often are structured as mortgage
- 13 refinancings or second mortgages. Approximately 70 percent of
- 14 subprime loans are for consumer credit card consolidation. Most
- 15 subprime loans are made by nondepository finance or mortgage



1 companies that are not subject to routine regulatory compliance  
2 review.

3 (c) Many subprime lenders offer a vital service to low-income  
4 borrowers who do not qualify for credit from mainstream financial  
5 institutions. However, many low-income borrowers have been  
6 victimized by improper subprime lending practices such as  
7 excessive fees and interest rates, repetitive refinancings, hidden  
8 costs, unnecessary insurance, and deceptive use of balloon  
9 payments. The abusive practices found in the subprime lending  
10 industry are referred to as predatory lending. Through misleading  
11 and deceptive sales practices, predatory lenders target cash-poor  
12 homeowners as customers for high-cost loans that often deprive  
13 these homeowners of the equity in their homes.

14 (d) It is the intent of the Legislature to improve consumers  
15 protection against predatory lending practices.

16 SEC. 2. Section 10247.5 is added to the Business and  
17 Professions Code, to read:

18 10247.5. No real estate broker or agent shall originate any  
19 high-cost loan by means of any manipulative, deceptive or other  
20 fraudulent scheme, device, or contrivance prohibited by the  
21 regulations adopted by the Secretary of the Business,  
22 Transportation and Housing Agency pursuant to Section 13984 of  
23 the Government Code. The commissioner shall enforce this  
24 section.

25 SEC. 3. Chapter 7.6 (commencing with Section 1922) is  
26 added to Title 4 of Part 4 of Division 3 of the Civil Code, to read:

27  
28 CHAPTER 7.6. LOANS SECURED BY REAL PROPERTY  
29

30 1922. (a) Notwithstanding any other provision of law, this  
31 section shall apply to all *subprime* residential mortgage loans and  
32 consumer loans secured by liens on real property made or serviced  
33 by a real estate broker or agent, a commercial or industrial bank,  
34 a savings association, or a finance lender.

35 (b) Section 1670.5 applies to the provisions of a loan contract  
36 that is subject to this section.

37 (c) A loan found to be unconscionable pursuant to Section  
38 1670.5 shall be deemed to be in violation of this section and subject  
39 to the remedies of this section.

1 (d) A lender, when making or negotiating a loan subject to this  
2 section, shall take into consideration in determining the size and  
3 duration of a loan, the financial ability of the borrower to repay the  
4 loan in the time and manner provided in the loan contract, and the  
5 ability of the borrower to refinance the loan at maturity.

6 (e) Escrow funds for a loan contract subject to this section shall  
7 be subject to and satisfy all applicable state and federal  
8 requirements, including Section 2609 of the Real Estate  
9 Settlement Procedures Act of 1974, as amended (12 U.S.C. Sec.  
10 2601 et seq.) and all applicable provisions of this code.

11 (f) Before any person may provide real estate brokerage  
12 services, as defined in Section 10131 of the Business and  
13 Professions Code, to a borrower for a loan contract subject to this  
14 section, the broker shall enter into a written loan brokerage  
15 contract with the borrower that satisfies the requirement of this  
16 section.

17 (g) The loan brokerage contract shall contain an explicit  
18 statement that the broker is acting as the agent of the borrower in  
19 providing brokerage services to the borrower, and when acting as  
20 agent for the borrower, the broker owes to that borrower a  
21 fiduciary duty of utmost care, honesty, and loyalty in the  
22 transaction, including the duty of full disclosure of all material  
23 facts. If the broker is authorized to act as an agent for any other  
24 person relative to the transaction, the loan brokerage contract shall  
25 contain a statement of that fact and identification of that person.

26 (h) The loan brokerage contract shall contain a detailed  
27 description of the services that the broker agrees to perform for the  
28 borrower, and a good faith estimate of any fees the broker will  
29 receive for those services, whether paid by the borrower, the  
30 institutional lender, or both.

31 (i) The loan brokerage contract shall include a clear and  
32 conspicuous statement of the conditions under which the borrower  
33 is obligated to pay the broker for brokerage services rendered  
34 under the contract.

35 (j) The loan brokerage contract shall provide that, if the broker  
36 makes a materially false or misleading statement or omission in the  
37 inducement or implementation of the contract, the borrower may,  
38 in addition to any other legal rights or remedies, upon written  
39 notice, do any of the following:

40 (1) Rescind the loan brokerage contract.

1 (2) Recover fees paid by the borrower to the broker for  
2 brokerage services rendered by the broker pursuant to the loan  
3 brokerage contract.

4 (3) Recover actual costs, including attorney's fees, for  
5 enforcing the borrower's rights under the loan brokerage contract.

6 (k) Any person who violates any provision of the federal Real  
7 Estate Settlement Procedures Act, as amended, or any regulation  
8 promulgated thereunder, violates this section *and shall be subject*  
9 *to the penalties and remedies provided for in that act. This*  
10 *subdivision shall be enforced by the agencies charged with*  
11 *administering Section 10247.5 of the Business and Professions*  
12 *Code and Sections 3398, 7508, 22168, and 50511 of the Financial*  
13 *Code.*

14 (l) Any person who violates any provision of the federal Truth  
15 in Lending Act, as amended, or any regulation promulgated  
16 thereunder, violates this section *and shall be subject to the*  
17 *penalties and remedies provided for in that act. This subdivision*  
18 *shall be enforced by the agencies charged with administering*  
19 *Section 10247.5 of the Business and Professions Code, and*  
20 *Sections 3398, 7508, 22168, and 50511 of the Financial Code.*

21 (m) The Secretary of the Business, Transportation and Housing  
22 Agency shall adopt regulations to implement this section and to  
23 define schemes, devices, or contrivances relating to the  
24 advertising, brokering, and making of loans subject to this section  
25 that are manipulative, deceptive or otherwise fraudulent.

26 (n) *Regulations adopted pursuant to this section shall prohibit*  
27 *predatory lending practices in the subprime market undertaken by*  
28 *lenders, brokers, or home improvement contractors, including, but*  
29 *not limited to, the following:*

30 (1) *The frequent making of new loans to refinance existing*  
31 *loans, also known as "flipping."*

32 (2) *The selling of additional products in a loan agreement*  
33 *without informed consent, also known as "packing."*

34 (3) *The making of loans without regard to the borrower's ability*  
35 *to repay.*

36 (4) *The charging of fees for services that bear no reasonable*  
37 *relationship to the value of services actually performed.*

38 (o) The regulations adopted under this section shall be enforced  
39 by the agencies charged with administering Section 10247.5 of the

1 Business and Professions Code and Sections 3398, 7508, 22168,  
2 and 50511 of the Financial Code.

3 ~~(o)~~

4 (p) If any provision of this section, *excluding subdivisions (k)*  
5 *and (l)*, is willfully violated in the making or collection of a loan,  
6 the contract of loan is void, and no person has any right to collect  
7 or receive any principal, charges, or recompense in connection  
8 with the transaction.

9 ~~(p)~~

10 (q) Any person who willfully violates any provision of this  
11 section or who willfully violates any rule or order adopted  
12 pursuant to this section, shall, upon conviction, be punished by a  
13 fine of not more than fifty thousand dollars (\$50,000), by  
14 imprisonment in a county jail for not more than one year or in the  
15 state prison, or by both that fine and imprisonment.

16 SEC. 4. Section 3398 is added to the Financial Code, to read:

17 3398. No commercial or industrial bank shall originate any  
18 high-cost loan by means of any manipulative, deceptive or other  
19 fraudulent scheme, device, or contrivance prohibited by the  
20 regulations adopted by the Secretary of the Business,  
21 Transportation and Housing Agency pursuant to Section 13984 of  
22 the Government Code. The commissioner shall enforce this  
23 section.

24 SEC. 5. Section 7508 is added to the Financial Code, to read:

25 7508. No savings association shall originate any high-cost  
26 loan by means of any manipulative, deceptive or other fraudulent  
27 scheme, device, or contrivance prohibited by the regulations  
28 adopted by the Secretary of the Business, Transportation and  
29 Housing Agency pursuant to Section 13984 of the Government  
30 Code. The commissioner shall enforce this section.

31 SEC. 6. Section 22168 is added to the Financial Code, to read:

32 22168. No finance lender shall originate any high-cost loan  
33 by means of any manipulative, deceptive or other fraudulent  
34 scheme, device, or contrivance prohibited by the regulations  
35 adopted by the Secretary of the Business, Transportation, and  
36 Housing Agency pursuant to Section 13984 of the Government  
37 Code. The commissioner shall enforce this section.

38 SEC. 7. Section 50511 is added to the Financial Code, to read:

39 50511. No residential mortgage lender shall originate any  
40 high-cost loan by means of any manipulative, deceptive or other

1 fraudulent scheme, device, or contrivance prohibited by the  
2 regulations adopted by the Secretary of the Business,  
3 Transportation and Housing Agency pursuant to Section 13984 of  
4 the Government Code. The commissioner shall enforce this  
5 section.

6 SEC. 8. Section 13984 is added to the Government Code, to  
7 read:

8 13984. (a) The Secretary of the Business, Transportation and  
9 Housing Agency, with respect to the origination of high-cost real  
10 estate loans, shall adopt regulations with respect to both of the  
11 following:

12 (1) Defining schemes, devices, or contrivances that are  
13 manipulative, deceptive, or otherwise fraudulent.

14 (2) Means to curb abusive practices related to the advertising,  
15 brokering, and making of high-cost loans, in order to protect  
16 consumers and the equity that homeowners have built up in their  
17 homes.

18 (b) *Regulations adopted pursuant to this section shall prohibit*  
19 *predatory lending practices in high-cost real estate loans*  
20 *undertaken by lenders, brokers, or home improvement*  
21 *contractors, including, but not limited to, the following:*

22 (1) *The frequent making of new loans to refinance existing*  
23 *loans, also known as “flipping.”*

24 (2) *The selling of additional products in a loan agreement*  
25 *without informed consent, also known as “packing.”*

26 (3) *The making of loans without regard to the borrower’s ability*  
27 *to repay.*

28 (4) *The charging of fees for services that bear no reasonable*  
29 *relationship to the value of services actually performed.*

30 (c) In developing the regulations under subdivision (a), the  
31 secretary shall consult with the Commissioner of Corporations, the  
32 Real Estate Commissioner, the Commissioner of Financial  
33 Institutions, and the Attorney General to ensure that the  
34 regulations appropriately address abusive high-cost lending  
35 practices.

36 ~~(e)~~

37 (d) The regulations adopted under this section shall be enforced  
38 by the agencies charged with administering Section 10247.5 of the  
39 Business and Professions Code and Sections 3398, 7508, 22168,  
40 and 50511 of the Financial Code.

1 SEC. 9. No reimbursement is required by this act pursuant to  
2 Section 6 of Article XIII B of the California Constitution because  
3 the only costs that may be incurred by a local agency or school  
4 district will be incurred because this act creates a new crime or  
5 infraction, eliminates a crime or infraction, or changes the penalty  
6 for a crime or infraction, within the meaning of Section 17556 of  
7 the Government Code, or changes the definition of a crime within  
8 the meaning of Section 6 of Article XIII B of the California  
9 Constitution.

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